

New Control on Global Debt: The International Lending Supervision Act of 1983

Ellen W. Smith

Follow this and additional works at: <http://scholarship.law.cornell.edu/cilj>



Part of the [Law Commons](#)

Recommended Citation

Smith, Ellen W. (1984) "New Control on Global Debt: The International Lending Supervision Act of 1983," *Cornell International Law Journal*: Vol. 17: Iss. 2, Article 7.

Available at: <http://scholarship.law.cornell.edu/cilj/vol17/iss2/7>

This Note is brought to you for free and open access by Scholarship@Cornell Law: A Digital Repository. It has been accepted for inclusion in Cornell International Law Journal by an authorized administrator of Scholarship@Cornell Law: A Digital Repository. For more information, please contact jmp8@cornell.edu.

NEW CONTROLS ON GLOBAL DEBT: THE INTERNATIONAL LENDING SUPERVISION ACT OF 1983

During the 1970s, commercial bank lending to developing countries grew at unprecedented rates, replacing other forms of investment as the main source of financing for their expanding economies.¹ External credit flows allowed developing countries to maintain high growth rates despite rising oil prices and balance-of-payments deficits,² but the growing debt gave rise to increased risk of future financial strains. In the early 1980s, global recession, rising interest rates, and a severe drop in commodity prices³ precipitated a series of debt-servicing problems, which quickly evolved into a worldwide financial crisis.⁴ By the end of 1982, the growth of international debt had reached such proportions that the disruption of debt service⁵ threatened the stability of the international financial system as well as the prospects for a global economic recovery.⁶

The buildup of international debt forced a reappraisal of commercial bank lending and of banking regulation. Regulatory supervision and controls had proved inadequate to prevent dangerous overlending by U.S. banks to developing countries.⁷ When Congress responded to the debt crisis with legislation in 1983, it sought not only to address the immediate liquidity problems of the distressed debtor countries but also to adopt long-range structural reforms for the international finan-

The author wishes to thank Walker F. Todd, member, New York Bar, for helpful comments on an earlier version of this Note. Any remaining errors are the responsibility of the author.

1. INTERNATIONAL MONETARY FUND, WORLD ECONOMIC OUTLOOK 25 (1983) [hereinafter cited as IMF, WORLD ECONOMIC OUTLOOK]. The term "developing countries" includes all countries except those classified as "industrial" or "oil exporting" countries by the International Monetary Fund (IMF). The oil exporting countries are essentially the members of the Organization of Petroleum Exporting Countries (OPEC). *See id.* at 168.

2. *Id.* at 5.

3. WORLD BANK, WORLD DEVELOPMENT REPORT 1983, at 8-12.

4. W. CLINE, INTERNATIONAL DEBT AND THE STABILITY OF THE WORLD ECONOMY 9-10 (1983).

5. "Debt service" is the payment of interest on short- and long-term debt plus installments of principal legally due on long-term debt. T. WALMSLEY, A DICTIONARY OF INTERNATIONAL FINANCE 67 (1979). The shortfall in debt service payments is known as "arrearages" or "arrearages."

6. *See infra* text accompanying note 15.

7. S. REP. NO. 122, 98th Cong., 1st Sess. 12-13 (1983). *See also infra* notes 25-38 and accompanying text.

cial system. The International Lending Supervision Act of 1983,⁸ passed as part of the debt crisis package,⁹ imposes new controls on foreign lending that are aimed at preventing a recurrence of the debt buildup.¹⁰

Section I of this Note examines the origins of the debt crisis and the need for improved controls on international lending. Section II discusses recent legislation intended to meet the crisis, the International Lending Supervision Act and the regulations promulgated thereunder. Section III analyzes the effect that the Act will have on short-term bank lending and on long-range structural reform of the international financial system.

I BACKGROUND

Following the sharp rise in world oil prices in 1973-74,¹¹ the external debt of the non-oil-exporting developing countries grew to unprecedented levels as these countries struggled to finance a growing balance-of-payments deficit.¹² At the same time, commercial banks, encouraged by high developing country growth rates in the 1960s and 1970s and pressed to invest oil exporting countries' surplus deposits, increased their lending to developing countries. From the mid-1970s to the early 1980s, commercial bank lending to developing countries grew at an annual rate of about twenty percent, comprising an ever-increasing proportion of developing-country financing.¹³

A. THE DEBT CRISIS OF THE 1980S

The second large oil price increase, which occurred in the late 1970s, was followed by a global recession in the 1980s, a dramatic fall

8. International Lending Supervision Act of 1983, Pub. L. No. 98-181, tit. IX, 97 Stat. 1278 (1983) (to be codified at 12 U.S.C. §§ 3901-3912) [hereinafter cited as ILSA].

9. Congress voted to increase the resources available to the IMF, as well as to reauthorize funds for the Export-Import Bank and other international development banks. See *infra* note 55 and accompanying text.

10. ILSA, § 902(a).

11. S. REP. NO. 122, *supra* note 7, at 3; see IMF, WORLD ECONOMIC OUTLOOK, *supra* note 1, at 46.

12. The external debt of the non-oil developing countries grew almost fivefold from 1973 to 1982 when it reached approximately \$612 billion. IMF, WORLD ECONOMIC OUTLOOK, *supra* note 1, at 200, table 32. The current payments deficit in the non-oil developing countries rose to \$69 billion by 1981, from an estimated level of \$2 billion in 1973. BANK FOR INTERNATIONAL SETTLEMENTS [BIS], ANNUAL REPORT, 1982, at 93; BIS, ANNUAL REPORT, 1976, at 61.

13. By mid-1982, bank loans to developing countries reached \$344 billion. R. DALE & R. MATTIONE, MANAGING GLOBAL DEBT 9 (1983). In 1971, bank loans accounted for only 13% of total medium- and long-term debt outstanding. By 1982, they provided 35%, the single largest source of medium- and long-term funds. *Id.* at 8.

in commodity prices, and accelerating interest rates.¹⁴ The resulting shortage of foreign exchange, exacerbated by a sudden contraction in credit flows to developing countries, brought about severe debt service problems, which threatened the stability of the international financial system. In late 1982 and 1983, approximately two-thirds of all bank debt owed by developing and Eastern European countries suffered a disruption of debt service or formal rescheduling.¹⁵ Strong action by the borrowing countries,¹⁶ supported by the International Monetary Fund (IMF), the international banking community, and the governments and central banks of many of the industrialized countries, kept the immediate liquidity crisis from escalating into massive default.¹⁷

The implications of this disruption in debt service for U.S. banks were severe. U.S. banks held approximately one-third of outstanding loans to developing countries.¹⁸ Moreover, the loans were highly concentrated, both by borrowing country and among lending banks. The nine largest U.S. banks had extended over sixty percent of these loans, which amounted to over twice their capital by mid-1982. The next fifteen largest U.S. banks accounted for an additional twenty percent. About half of the loans were to Mexico, Argentina, and Brazil.¹⁹

14. See generally IMF, RECENT MULTILATERAL DEBT RESTRUCTURINGS WITH OFFICIAL AND BANK CREDITORS, OCCASIONAL PAPER No. 25 (1983) (origins of the crisis); W. CLINE, *supra* note 4. In 1980, commodity prices fell 30%, to their lowest levels in years, while the volume of world trade declined for only the second time in the postwar era. S. REP. NO. 122, *supra* note 7, at 4. For a discussion of commodity price developments, see IMF, WORLD ECONOMIC OUTLOOK, *supra* note 1, at 154-59.

15. W. CLINE, *supra* note 4, at 10.

16. The major distressed debtor countries adopted stringent economic adjustment measures at the behest of the IMF and the lending banks. On the austerity measures of Mexico and Brazil, see M. MENDELSON, COMMERCIAL BANKS AND THE RESTRUCTURING OF CROSS-BORDER DEBT (1983).

17. On the financial rescue packages put together in 1982-83, see IMF, RECENT MULTILATERAL DEBT RESTRUCTURINGS, *supra* note 14; W. CLINE, *supra* note 4, at 40-44. The packages included economic adjustment measures, an IMF program, additional bank lending, and official bridging loans (short-term loans that enable a borrower to service existing loans until a debt rescheduling can be arranged). *Id.* at 40.

18. In mid-1982, U.S. banks had extended \$99 billion in loans to developing countries, excluding OPEC and Eastern European borrowers. *International Financial Markets and Related Problems: Hearings Before the House Comm. on Banking, Finance, and Urban Affairs*, 98th Cong., 1st Sess. 71, table II (1983) [hereinafter cited as *International Financial Markets and Related Problems*] (statement of Paul A. Volcker, chmn., Bd. of Gov., Fed. Res. Sys.).

19. *Id.* at tables II-IV.

Compounding this concentration was the fact that most of the increase over this period was in the form of short-term credits. While they seemed less risky than medium- and long-term credits and while they were attractive to the LDC's [less-developed countries] in times of high interest rates, they also increased the borrowers' vulnerability to a sudden reduction in the willingness of lenders to roll over existing debt. Moreover, short-term lending provided little protection for the banks as a group, since they could not all attempt to withdraw such credit at the same time without provoking a liquidity crisis for the borrowers.

S. REP. NO. 122, *supra* note 7, at 4-5.

A number of factors contributed to the high lending concentrations of the large international banks. Economic motives were the most prominent factor. Banks simply responded to lending opportunities and to the advantages of developing a relationship with a particular country.²⁰ Other contributing factors included inadequate information on borrowing countries' total indebtedness, internal pressures generated by bank lending officer performance evaluations, and competition among lenders for continued relationships with borrowers.²¹ The overexposure resulting from these and other factors lead one study to conclude: "The lesson to be learned from recent events . . . is that the market cannot be . . . relied on . . . to impose a prudent ceiling on the indebtedness of individual countries."²²

The high lending concentrations in individual countries placed the largest U.S. banks in a potentially vulnerable position. High concentrations not only expose banks to the risk of a larger default but also may put excessive bargaining power into the hands of borrowers.²³ Holders of large claims generally will agree readily to reschedule or modify terms of repayment. Lenders are also more willing to extend new credit to protect outstanding loans. Moreover, if the amount of new credit needed to protect the outstanding loans becomes greater than the bank's unimpaired capital, affecting the bank's insurers' and possibly its creditors' interests, the borrowers gain even more bargaining power.²⁴

B. THE INADEQUACY OF PRIOR INTERNATIONAL LENDING SUPERVISION

Banking industry observers first expressed concern about the stability of the banking system in the mid-1970s, as they witnessed a rising number of bank failures.²⁵ They also voiced warnings about the sudden increases in international debt and the development of danger-

20. For an analysis of these and other factors contributing to the banks' heavy concentrations of country exposure, see *To Increase the U.S. Quota in the International Monetary Fund and Related Matters: Hearings Before the Subcomm. on International Trade, Investment, and Monetary Policy of the House Comm. on Banking, Finance, and Urban Affairs*, 98th Cong., 1st Sess. 186-92 (1983) [hereinafter cited as *To Increase the U.S. Quota*] (paper by Jack Guttentag and Richard Herring).

21. *Id.*

22. R. DALE & R. MATTIONE, *supra* note 13, at 24-25.

23. This reflects the adage that "a large enough debt turns a creditor into a partner." Huff, *The Rescheduling of Country Debt: Is a More Formalized Process Necessary?*, reprinted in GROUP OF THIRTY, RISKS IN INTERNATIONAL BANK LENDING 52 (1982).

24. For an analysis of the danger of high country concentration exposure, see Guttentag & Herring, *Uncertainty and Insolvency Exposure by International Banks*, 4 BROOKINGS DISCUSSION PAPERS IN INTERNATIONAL ECONOMICS (1983); GROUP OF THIRTY, RISKS OF INTERNATIONAL BANK LENDING, *supra* note 23.

25. H.R. REP. NO. 175, 98th Cong., 1st Sess. 31 (1983).

ous ratios of deposits and credits to capital.²⁶ In 1977, the General Accounting Office (GAO) issued a report that revealed inconsistencies among and within the federal banking agencies²⁷ regarding the supervision of foreign lending. The report also identified inadequate controls on foreign lending within banks.²⁸

The federal banking agencies subsequently took steps to improve supervision of foreign lending. In late 1977, they instituted the Country Lending Exposure Survey, a semi-annual report designed to collect information on loans to foreign borrowers.²⁹ The Interagency Country Exposure Review Committee (ICERC), established in 1979, devised a uniform system for evaluating the unique risks in international banking, which were not accounted for under previous bank examination procedures.³⁰ In particular, the ICERC was to review "transfer risk"³¹ and to categorize the credit standing of individual country borrowers. Examiners were to consider these credit classifications when determining prudent country exposure levels for individual banks and when formulating comments and recommendations for their examination reports.³²

The ICERC evaluations were purely advisory, however, and they ultimately proved ineffective in light of the debt service crisis of

26. *Id.* at 32; *Burns Warns Banks on LDC Lending Pace*, *The Am. Banker*, March 11, 1977, at 1, col. 5. Bank failures and near-failures in Germany and England indicated that European supervisory controls might also be inadequate to cope with new patterns of international finance. *Id.* See also Becker, *International Insolvency: The Case of Herstatt*, 62 A.B.A. J. 1290 (1976) (collapse of the German international bank in 1974).

27. The federal banking agencies are the Office of the Comptroller of the Currency (OCC), the Board of Governors of the Federal Reserve System, and the Federal Deposit Insurance Corporation (FDIC). State banking departments also supervise banks chartered within their borders. No single banking regulatory agency has the authority or responsibility to oversee international lending.

28. GAO, *FEDERAL SUPERVISION OF STATE AND NATIONAL BANKS* (1977).

29. The Federal Financial Institutions Examination Council publishes the Country Exposure Report (Form FFIEC 009) in aggregate form. The report includes data on cross-border loans not repayable in local currency and not subject to third country guaranties. See *International Financial Markets and Related Problems*, *supra* note 18, at 385-86 (1983) (statement of Richard Dale, guest scholar, The Brookings Inst.); *A New Supervisory Approach to Foreign Lending*, FED. RES. BANK N.Y.Q. REV., Spring 1978, at 1.

30. For a description of the country risk evaluation program instituted by the ICERC, see *International Financial Markets and Related Problems*, *supra* note 18, at app. II, 84-89 (statement of Paul A. Volcker).

31. Transfer risk is the possibility that a borrower will not be able to maintain debt servicing in the currency in which the debt is to be repaid because of a lack of foreign exchange in the borrower's country, irrespective of the borrower's own financial position. See *id.* Such a risk is unique to international lending. Cf. Allocated Transfer Risk Reserve Regulations 49 Fed. Reg. 5587, 5592 (1984) (to be codified at 12 C.F.R. pts. 20, 211, 351) [hereinafter cited as ATRR Regulations] (definition of transfer risk).

32. See *International Financial Markets and Related Problems*, *supra* note 18, at app. II, 84-89 (statement of Paul A. Volcker).

1982.³³ Loan concentrations had continued to grow, especially in lending to Latin America.³⁴ Banks had also failed to increase sufficiently provisioning for loans to countries in difficulty.³⁵ While the large U.S. banks began to increase their loan loss reserves in 1982, increases and total reserves lagged well behind those of banks in other major lending countries.³⁶

Both legislators and banking regulators recognized that current measures were inadequate to reduce overextension in foreign lending. Legislators pointed to a failure of regulatory and supervisory controls to monitor international lending and to prevent unsound concentrations of country exposure. Moreover, they cited lack of enforcement by regulatory agencies, which had robbed existing requirements of any strength.³⁷ In congressional testimony, FDIC Chairman William M. Isaac stated, "[A]s bank supervisors, we failed to effectively caution American banks to restrain foreign lending growth. Although portfolio concentrations were identified and commented upon, sufficiently firm steps were not taken to limit concentrations and the leveraging of bank capital. Without question our supervisory efforts need buttressing."³⁸

33. A follow-up report issued by the GAO in 1982 found that "comments by bank examiners have had little impact in restraining the growth of . . . [bank] exposures." GAO, *BANK EXAMINATION FOR COUNTRY RISK AND INTERNATIONAL LENDING* iv (1982). The report identified a number of other weaknesses in the system, including a lack of consistency in highlighting the special comments; identification of too many "problem countries," thereby diminishing the impact of comments; and inadequate analysis in the risk-evaluation stage of the system. *Id.* Richard Dale notes, for example, that for the purpose of evaluating country lending exposures, capital funds are defined to include subordinated debt and loan loss reserves, producing lower country exposure figures than those derived based on published equity capital. *International Financial Markets and Related Problems*, *supra* note 18, at 387 n.4.

34. By mid-1982, loans to Mexico, Argentina, and Brazil, made by the nine largest U.S. banks, reached almost 140% of their combined equity capital. H.R. REP. NO. 175, *supra* note 25, at 36. Loans to all non-OPEC developing countries reached 270% of the nine banks' combined capital. *Id.* See generally *International Financial Markets and Related Problems*, *supra* note 18, at 386-91 (statement of Richard Dale).

35. In 1982, the nine largest U.S. banks had reserves amounting to 1.7% of the value of their total loans outstanding to eleven countries that had recently experienced a disruption in debt service. W. CLINE, *supra* note 4, at 98.

36. In the second half of 1982, the largest U.S. banks increased loan loss reserves by 55% or less over 1981, while comparable British banks increased reserves by 200%. See *To Increase the U.S. Quota*, *supra* note 20, at 494 (statement of Karin Lissakers, resident assoc., Carnegie Endowment for Int'l Peace, former Deputy Dir. for Policy Planning, Dep't of State).

37. H.R. REP. NO. 175, *supra* note 25, at 30-37.

38. *International Bank Lending: Hearings Before the Subcomm. on Financial Institutions Supervision, Regulation, and Insurance of the House Comm. on Banking, Finance, and Urban Affairs*, 98th Cong., 1st Sess. 210 (1983) [hereinafter cited as *International Bank Lending*] (statement of Hon. William M. Isaac, chmn., FDIC and Fed. Fin. Inst. Examin. Council). Cf. The Am. Banker, *supra* note 26 (Burns' warning).

II CONGRESSIONAL RESPONSE

Congress initially responded to the debt crisis with two related measures. With Administration support, some legislators sought to authorize an \$8.4 billion increase in U.S. participation in the International Monetary Fund in order to fulfill a general quota increase voted by Fund members in 1982.³⁹ The IMF bill came under sharp attack in Congress as a "big bank bailout."⁴⁰ Critics contended that IMF loans to distressed countries merely go to pay interest on debts to large commercial banks.⁴¹ Supporters of the increase sought to mollify the opposition by tying it to legislation requiring tougher supervision and restrictions on foreign lending by U.S. banks.⁴²

A. MOTIVES FOR REFORM

The congressional banking committees convened hearings in late 1982 and early 1983 on the role of U.S. banks in the international debt crisis.⁴³ Various groups exhibited divergent goals by offering their views of and remedies for the problem. Some legislators saw tougher restrictions on banks as a quid pro quo for what they or their constituents perceived as a bonus for big banks.⁴⁴ Others agreed to support restrictions in order to obtain passage of the IMF increase.⁴⁵ Still others cautioned against seeking retribution from U.S. banks and against overreacting to the problem.⁴⁶

While banking regulators agreed that more effective controls were advisable, they emphasized the need for flexibility in applying new safeguards in order not to jeopardize short-term commercial credit flows to borrowers in difficulty. Federal Reserve Board Chairman Paul A. Volcker warned that the sudden imposition of stiff regulatory measures might induce "abrupt action by lenders to withdraw from

39. 1983 CONG. Q. 2488 (Nov. 26). The increase represented a 50% increase in members' quotas; at current rates of drawings, however, further increases will be necessary in late 1984 or early 1985. See *To Increase the U.S. Quota*, *supra* note 20, at 488-89 (statement of Karin Lissakers).

40. H.R. REP. NO. 175, *supra* note 25, at 25-26.

41. *Id.*

42. See 41 WASH. FIN. REP. (BNA) No. 5, at 144-45 (Aug. 1, 1983); *To Increase the U.S. Quota*, *supra* note 20, at 488-89 (statement of Karin Lissakers).

43. S. REP. NO. 122, *supra* note 7, at 10-11; H.R. REP. NO. 175, *supra* note 25, at 38.

44. See *Proposed Solutions to International Debt Problems: Hearing Before the Senate Comm. on Banking, Housing, and Urban Affairs*, 98th Cong., 1st Sess. 6 (1983) [hereinafter cited as *Proposed Solutions to International Debt Problems*] (remarks of Sen. Heinz) ("The price of [an] \$8.4 billion increase in the Congress is going to be [international banking supervision] legislation.").

45. See *Proposed Solutions to International Debt Problems*, *supra* note 44, at 95 (statement of Sen. Garn, chmn.).

46. Senator Garn cautioned legislators to bear in mind the problems that could result from over-regulation. *Id.* at 2.

lending . . . which would precipitate financial crises in otherwise creditworthy countries."⁴⁷ Regulators insisted that reforms could be introduced without new enabling legislation, but members of Congress doubted the effectiveness of purely regulatory measures.⁴⁸ Some industry observers also questioned the ability and willingness of regulators to take a tougher stand without legislative backing.⁴⁹

Responding to congressional pressure, the federal banking agencies presented a joint memorandum to Congress proposing reforms of the supervision and regulation of international lending.⁵⁰ The proposal, which became the cornerstone of draft legislation,⁵¹ consisted of measures to:

- (1) strengthen existing procedures for country risk examination and evaluation;
- (2) increase collection and public disclosure of data on banks' country exposures;
- (3) establish a system of special reserves for problem foreign loans;

47. *Proposed Solutions to International Debt Problems*, *supra* note 44, at 9; *International Financial Markets and Related Problems*, *supra* note 18, at 214 (testimony of William S. Ogden, vice chmn., Chase Manhattan Bank) ("[T]he extent to which the international banking system can contribute to the future resolution of the debt problem is directly related to the extent of the penalty now being paid by the banks for their past decisions To add to [the penalty] through new administrative measures would diminish the capability of banks to furnish needed credits").

Yet another interested party, the Securities and Exchange Commission, concerned primarily with protection of investors, focused on reforms to reflect more clearly the effect of international lending on the financial position of bank holding companies. *See International Bank Lending*, *supra* note 38, at 350 (statement of John S.R. Shad, chmn., SEC). In 1982, the SEC instituted additional foreign loan disclosure requirements for bank holding companies in SEC filings. *See infra* note 69 and accompanying text. The tension between the SEC and the banking regulatory agencies over the type and amount of information banks should be required to disclose is a result of the different missions of the agencies—protection of investors versus protection of the soundness and stability of the banking system. *See Guttentag & Herring, Disclosure Policy and International Bank Lending*, 7 BROOKINGS DISCUSSION PAPERS IN INTERNATIONAL ECONOMICS 3-4 (1983).

48. *See Proposed Solutions to International Debt Problems*, *supra* note 44, at 7 (statement of Sen. Proxmire).

49. "[R]egulatory compromises which have been made to accommodate the banks during the current emergency" could hamper regulators' efforts to impose stricter requirements. *To Increase the U.S. Quota*, *supra* note 20, at 492 (statement of Karin Lissakers).

The Senate Banking Committee also mentioned in its report of S. 695 the need to clarify the existing authority of the banking agencies to establish and enforce appropriate capital levels for banks under their jurisdiction. S. REP. NO. 122, *supra* note 7, at 16. In a recent decision, the United States Court of Appeals for the Fifth Circuit set aside the Comptroller's capital requirement for a national bank. *First Nat'l Bank of Bellaire v. Comptroller of the Currency*, 697 F.2d 674, 686 (5th Cir. 1983).

50. Board of Governors of the Federal Reserve System, FDIC, and Comptroller of the Currency, Joint Memorandum: Program of Improved Supervision and Regulation of International Lending (Apr. 7, 1983), *reprinted in Proposed Solutions to International Debt Problems*, *supra* note 44, at 24 [hereinafter cited as Joint Memorandum].

51. The proposal was resubmitted in the form of draft legislation at the request of the Senate Banking Committee. S. REP. NO. 122, *supra* note 7, at 11.

- (4) require procedures to account for rescheduling and front-end fees⁵² over the life of a foreign loan; and
- (5) strengthen international cooperation with foreign banking regulators and through the IMF.

House and Senate bills incorporated the agencies' proposal and an appropriation for the IMF quota increase.⁵³

B. THE INTERNATIONAL LENDING SUPERVISION ACT OF 1983

After a year-long struggle to obtain passage of the IMF funding increase,⁵⁴ Congress enacted an eleventh-hour compromise package in November 1983.⁵⁵ The package authorized an \$8.4 billion increase in U.S. funding to the IMF and provided for increased regulation of foreign loans by commercial banks under the International Lending Supervision Act.⁵⁶ The Act requires the banking regulatory agencies to tighten capital and reserve requirements, increase information collection and disclosure, and modify accounting practices in order to reduce artificial incentives to engage in foreign lending. It allows the agencies to exercise discretion, however, in framing regulations and in fixing requirements for individual banks.

1. *Capital Adequacy and Evaluation*

Several provisions of the Act are designed to ensure adequate capital levels for banks engaged in international lending. The Act requires the federal banking agencies to establish minimum capital levels, which may be raised for individual banks at the discretion of the appropriate agency. The Act specifies that a failure to meet the established levels may be deemed an unsafe and unsound practice.⁵⁷

52. A front-end fee is a flat fee paid by the borrower to the lending bank on the signing or disbursement date of a loan. Also called a "commission," "financing fee," or "flat fee," it is generally calculated as a percentage of the credit and "in most instances represent[s] an adjustment to the interest yield" of the loan. Joint Memorandum, *supra* note 50, at 49, 51.

53. H.R. 2957, 98th Cong., 1st Sess., tit. IV (1983), reprinted in H.R. REP. NO. 175, *supra* note 25, at 9; S. 695, 98th Cong., 1st Sess. (1983).

54. See *supra* notes 39-42 and accompanying text.

55. H.R. 3959, 98th Cong., 2d Sess. (1984). The hybrid legislation included a major housing appropriations bill, along with reauthorizations for the Export-Import Bank and other international development banks. Congress broke all procedural rules to pass the measure, which was incorporated as an amendment to the conference report of a fiscal 1984 supplemental appropriations bill. *Id.* The Senate approved the amendment on November 17, with minor changes, 129 CONG. REC. S16,538 (Nov. 17, 1983), and the House concurred the following day, 129 CONG. REC. H10,529 (Nov. 18, 1983). Supplemental Appropriations Act, 1984, Pub. L. No. 98-181, 97 Stat. 1153 (1983).

56. International Lending Supervision Act of 1983, Pub. L. No. 98-181, tit. IX, 97 Stat. 1278 (1983) (to be codified at 12 U.S.C. §§ 3901-3912).

57. ILSA, § 908. A finding that a bank is engaged in an "unsafe and unsound practice" may result in loss of FDIC-insured status. 12 U.S.C. § 1818 (1982). Until June 1983, minimum capital requirements were not prescribed for the seventeen "multinational" banks under the jurisdiction of the Federal Reserve Board. Capital-to-asset ratios for the largest multinational banks had dropped to levels of 4-5% during the 1970s, compared to

The Act directs the banking agencies to incorporate two factors, foreign country exposure and transfer risk, into their general examination procedures and particularly into their evaluations of capital adequacy.⁵⁸ In their joint memorandum to Congress, the banking agencies had outlined their intention to incorporate these factors more effectively into examination procedures. The agencies had defined new loan classification categories to include transfer risk, which will affect bank asset-quality ratings.⁵⁹ The proposal also had included country exposure concentrations in bank capital-adequacy evaluations.⁶⁰

2. Reserves

The Act requires banks to set aside special loan loss reserves for loans to countries that, in the judgment of the banking agency, are subject to a high level of transfer risk. Banks are to charge the reserves against current income and may not consider them part of the bank's capital or other required loan loss reserves.⁶¹ Charging reserves against current income gives the reserves the effect of a write-off. The Act requires the banking agencies to consider certain factors, such as a borrower's failure to make interest payments or to comply with IMF adjustment programs, in determining the applicability of the reserve requirement.⁶² Legislators, however, dropped provisions

the minimum level of 6% or more required for banks with less than \$1 billion in assets. Likewise, the FDIC, while maintaining a minimum capital requirement of 5% for banks under its authority, did not enforce the standard for larger banks. See H.R. REP. NO. 175, *supra* note 25, at 45. The large banks began increasing capital levels in the second half of 1982, see S. REP. NO. 122, *supra* note 7, at 13, and in June, 1983, the Federal Reserve issued fixed minimum standards of 5% for multinational banks for the first time, see *Minimum Capital Guidelines: Amendments*, 69 FED. RES. BULL. 539 (1983). The Act does not require the establishment of a single, uniform standard for all banks, but the Senate Banking Committee commented in its report that "the Committee expects the standards developed under this Act will be uniform among the three bank regulatory agencies, so that banks with the same characteristics are treated alike regardless of their regulatory status." S. REP. NO. 122, *supra* note 7, at 16.

58. ILSA, § 904.

59. Joint Memorandum, *supra* note 50, at app. A, 34-35.

60. *Id.*

61. ILSA, § 905.

62. Section 905(a)(1) provides:

Each appropriate Federal banking agency shall require a banking institution to establish and maintain a special reserve whenever, in the judgment of such appropriate Federal banking agency—

(A) the quality of such banking institution's assets has been impaired by a protracted inability of public or private borrowers in a foreign country to make payments on their external indebtedness as indicated by such factors, among others, as—

(i) a failure by such public or private borrowers to make full interest payments on external indebtedness;

(ii) a failure to comply with the terms of any restructured indebtedness; or

(iii) a failure by the foreign country to comply with any International Monetary Fund or other suitable adjustment program; or

requiring the establishment of reserves for virtually all foreign loans, and in particular, for all rescheduled loans, from the final version.⁶³

Pursuant to regulations promulgated under the Act, the federal banking agencies jointly determine which assets they will designate reservable.⁶⁴ In their joint memorandum to Congress, the regulators defined new loan classification categories, "reservable" and "debt-service impaired," to replace the traditional categories of "substandard" and "doubtful."⁶⁵ Reservable loans are those impaired by a protracted inability of public or private obligors in a foreign country to make payments, or are those made to borrowers in countries where there are no definite prospects for the orderly restoration of debt service.⁶⁶ The regulations establish an initial guideline for Allocated Transfer Risk Reserves (ATRRs) in an amount equal to ten percent of each loan classified as reservable, subject to additional annual increases of fifteen percent as warranted.⁶⁷

3. *Information Collection and Disclosure*

The Act increases reporting and disclosure requirements for foreign country exposure.⁶⁸ Banking institutions must report their foreign lending exposure to the appropriate banking agency on a quarterly rather than the former semi-annual basis. The Act also requires public disclosure of information regarding material foreign country exposure.⁶⁹ The reporting requirements will provide a profile of aggregate country lending data by sector and maturity distribution and will provide information on U.S. government guaranties.⁷⁰

(B) no definite prospects exist for the orderly restoration of debt service.

63. See S. REP. NO. 122, *supra* note 7, at 14.

64. ATRR Regulations, *supra* note 31.

65. Joint Memorandum, *supra* note 50, at app. A, 34-35, app. C, 40-44. Loans placed in the loss category, which remains unchanged, are defined as completely uncollectible (for example, repudiated debt) and will be written-off. *Id.* at 35.

66. See ILSA, § 905(a)(1).

67. ATRR Regulations, *supra* note 31. The regulations also establish a write-off option for designated assets in lieu of establishing an ATRR. See also S. REP. NO. 122, *supra* note 7, at 14.

68. ILSA, § 907.

69. Revisions to the present Country Exposure Report proposed by the Federal Financial Institutions Examination Council would define material foreign country exposures as those exceeding 1.0% of a reporting bank's assets. Less detailed information would be required on exposures exceeding 0.75% but not exceeding 1.0% of assets. Quarterly Report of Country Exposure by U.S. Banking Organizations, 48 Fed. Reg. 56,848, 56,849 (1983) (request for comments) [hereinafter cited as Quarterly Report of Country Exposure]. The standard of materiality corresponds to the standard adopted by the SEC in its new disclosure requirements. SEC, Staff Accounting Bulletin No. 49, 47 Fed. Reg. 49,627 (1982); SEC, Staff Accounting Bulletin No. 49A, 48 Fed. Reg. 3585 (1983). See *supra* note 47.

70. Quarterly Report of Country Exposure, *supra* note 69, at 56,849.

4. *Accounting for Fees*

Several provisions of the Act require new accounting treatment for fees charged in connection with international loans. The Act prohibits a bank from charging loan restructuring fees that exceed the bank's administrative costs unless the fee is amortized over the life of the loan.⁷¹ The federal banking agencies must establish regulations for accounting for front-end fees charged in connection with international credits over the life of a loan.⁷² In the past, some banks recognized front-end fees as current income rather than amortizing the portion representing interest over the life of the loan. This practice increased earnings and created an artificial incentive to engage in international lending.⁷³ The new accounting procedures assure that any portion of front-end fees that does not represent direct costs will be fully amortized.⁷⁴

5. *Other Provisions*

The remaining provisions of the Act call for international cooperation to coordinate banking regulatory activity with supervisory policies in other countries,⁷⁵ and require bank lending officers to submit economic feasibility evaluations to bank management for certain large foreign loans.⁷⁶ The Act gives the GAO audit authority to monitor the banking agencies' compliance⁷⁷ and mandates subsequent reports to Congress by the banking agencies.⁷⁸

III ANALYSIS

The question remains whether the International Lending Supervision Act will induce the long-range structural reforms necessary to solve the problem of excessive country concentrations and overexten-

71. ILSA, § 906(a).

72. *Id.* § 906(b). *See supra* note 52.

73. *See* Accounting for International Loan Fees, 49 Fed. Reg. 12,192, 12,195 (1984) (to be codified at 12 C.F.R. pts. 20, 211, 351).

74. *Id.* at 12,192-99. The Financial Accounting Standards Board is considering establishing standards on the subject; generally accepted accounting principles (GAAP) do not now provide for accounting for loan fees. *See id.* at 12,193.

The banking agencies' proposed rules would have applied equally to loan restructuring fees and those associated with other international loans. ATRR Regulations, *supra* note 31, at 5594. The final rules, however, allow banks to charge some syndicated loan fees and commitment fees on non-restructured international loans when the loans are initiated.

75. ILSA, § 902(2).

76. *Id.* § 909. Section 909, added by H.R. 2957 but passed with considerably less stringent provisions, requires banks to prepare economic evaluations for foreign loans exceeding \$20 million for mining or metalworking projects. A senior bank official must approve each evaluation. Federal bank examiners will routinely review the evaluations.

77. *Id.* at § 911.

78. *Id.* at § 913.

sion by U.S. banks.⁷⁹ The regulations are clearly prospective; they are not designed to alleviate the immediate liquidity crisis. Their effectiveness should therefore be evaluated in terms of their long-range impact. The goal of reform should be to establish adequate prior controls on lending to prevent a recurrence of the crisis. An examination of the International Lending Supervision Act, however, reveals little substantive regulatory reform and even less of a solution to the international debt problem.

A. MINIMAL RESTRICTIONS ON FOREIGN LENDING

Earlier versions of the legislation provided for tougher restrictions on foreign lending.⁸⁰ Banking regulators and industry analysts warned, however, against stopping short-term commercial credit flows to distressed countries. They asserted that these credits might be jeopardized if legislators were to place more stringent controls on banks.⁸¹ According to regulators, resolution of the *immediate* liquidity crisis calls for more, not less, lending. Consequently, they urged that reforms should be tempered to minimize short-term effects on private credit flows.⁸²

Banking regulators and other analysts also cited problems of competition in calling for legislative restraint. Differences in supervi-

79. See *supra* notes 18-19 and accompanying text.

80. Chief among these restrictions was the proposal to impose country lending limits embodied in S. 502 (the Heinz-Proxmire bill), 98th Cong., 1st Sess. (1983), reprinted in *Proposed Solutions to International Debt Problems*, *supra* note 44, at 97, and also in H.R. 2957, *supra* note 53. The banking agencies and some analysts strongly opposed these on the basis of differences among countries, political pressures, and the fact that banks' exposure in some countries was already high. For the debate on country lending limits, see *International Financial Markets and Related Problems*, *supra* note 18, at 55 (statement of Paul A. Volcker); *To Increase the U.S. Quota*, *supra* note 20, at 224-28 (paper by Jack Guttentag and Richard Herring); *id.* at 497-99 (statement by Karin Lissakers); *Proposed Solutions to International Debt Problems*, *supra* note 44, at 83-84; R. DALE & R. MAT-TIONE, *supra* note 13, at 34-35.

H.R. 2957, *supra* note 50, would also have imposed special reserve requirements for all rescheduled loans. Critics maintained that this kind of requirement might jeopardize restructuring efforts and result in "regulatory overkill." See W. CLINE, *supra* note 4, at 99; *Proposed Solutions to International Debt Problems*, *supra* note 44, at 91. See generally GROUP OF THIRTY, RISKS IN INTERNATIONAL BANK LENDING, *supra* note 23, at 213-14.

81. Regulators repeatedly emphasized the need for flexibility in resolving the current crisis while implementing long-range reforms. See *Proposed Solutions to International Debt Problems*, *supra* note 44, at 16 (statement of Paul A. Volcker). Others question, however, the desirability of continued commercial short-term balance of payments financing. See *infra* notes 101-03 and accompanying text.

82. "[O]nce high exposures are a fact of life, . . . the menu of available remedies is more limited and some remedies aimed at preventing excessive exposure may be counterproductive." Guttentag & Herring, *supra* note 24, at 50. Furthermore, if lines of credit were cut off or reduced, forcing a reduction in scheduled interest payments, the result could cause even greater harm to the soundness of the banking system the legislators wanted to protect. See Maroni, *A Strategy to Resolve Mexico's Liquidity Crisis*, 228 INTERNATIONAL FINANCE DISCUSSION PAPERS 11 (1983).

sory systems in other countries result in competitive disadvantages for banks. Regulatory differences may encourage banks to locate their lending activities where capital requirements are less stringent.⁸³ In addition, borrowers may prefer to deal with institutions that are not subject to public disclosure requirements.⁸⁴ On the other hand, one commentator argues that "the U.S. should [not] set its standards according to the lowest common denominator just to protect the competitive position of U.S. banks."⁸⁵ Other commentators endorse the theory that one country must take the lead in setting stricter regulatory requirements, relying on greater international cooperation to encourage other countries to adopt similar standards.⁸⁶ These commentators recognize that without more stringent requirements, there will not be an effective solution to the current international debt problem.

B. CHANGES IN ACCOUNTING PROCEDURES

Some of the changes in accounting procedures under the Act make needed modifications in accounting for foreign lending. Other provisions, however, will not have enough effect to modify bank lending behavior. The Act's special reserve requirements for loans to countries that are experiencing payment difficulties will, in the short-term, appear to have little effect on bank balance sheets. The criteria for classifying loans in the reservable category were scaled to an extremely high level of distress in order not to interfere with current commercial credit flows, particularly those initiated under IMF auspices. According to industry analysts, the reserve requirements will only affect loans to a few countries with very minor amounts of debt outstanding to U.S. banks.⁸⁷ Most banks have already written off substantial portions of the loans involved.⁸⁸

The extent to which the special reserve requirements will effect desired long-term structural reforms is uncertain. In terms of induc-

83. See Guttentag & Herring, *supra* note 24, at 45-46; Bryant, *Eurocurrency Banking: Alarmist Concerns and Genuine Issues*, 2 BROOKINGS DISCUSSION PAPERS IN INTERNATIONAL ECONOMICS 46 (April 1983). But cf. *To Increase the U.S. Quota*, *supra* note 20, at 495 (statement of Karin Lissakers) (protecting competitive position of U.S. banks should not control capital adequacy decisions).

84. See Guttentag & Herring, *Disclosure Policy and International Banking*, 7 BROOKINGS DISCUSSION PAPERS IN INTERNATIONAL ECONOMICS 16 (December 1983).

85. *To Increase the U.S. Quota*, *supra* note 20, at 495 (statement of Karin Lissakers).

86. See, e.g., *International Bank Lending*, *supra* note 38, at 338-39 (statement of J. Charles Partee, Bd. of Gov., Fed. Res. Sys.).

87. Sources indicated that new reserves would be required for loans to Zaire (equal to 75% of principal outstanding); Sudan (50%); Poland and Nicaragua (15%); and Bolivia (10%). The amount of reserves required is less than 6% of the nine largest U.S. banks' 1982 pre-tax earnings. Wall St. J., Dec. 27, 1983, at 2, col. 3.

88. *Id.*

ing banks to increase capital levels, one study concluded that there would be little incentive because banks' true capital would remain unaffected by the new write-off.⁸⁹ Regulators would be able to force banks to increase capital levels only when the required reserves brought capital levels below the statutory minimum.⁹⁰ It is possible that at some point the reserve requirements might be applied to a larger debtor country whose situation had deteriorated. Requiring U.S. banks to set aside reserves equal to ten percent of loans to Mexico or Brazil,⁹¹ for example, would have a more extreme impact on bank capital.⁹²

On the other hand, some regulators have warned that the reserve requirements may not go far enough to protect adequately against loan losses.⁹³ The SEC has warned bank holding companies that the amount allocated to meet transfer risk reserve requirements may not be enough to meet the requirements of generally accepted accounting principles (GAAP) for prudent loan loss reserves.⁹⁴ At a minimum, however, the reserves should have some cushioning effect for large losses in the event the problem loans are not repaid.

The new requirements for accounting for loan fees will provide uniform accounting procedures and require the amortization of any portion of the fee that is not a reimbursement of direct costs. These reforms are consistent with good accounting practice. The new accounting methods will cause only a short-term reduction in bank earnings, until the changeover is complete.⁹⁵ The amortization requirement, however, may eliminate any artificial incentive to boost earnings by engaging in foreign loans with high front-end fees attached. In this respect, the Act encourages banks to exercise restraint in exposing themselves to country risk.⁹⁶

89. See *supra* note 61 and accompanying text. See also Guttentag & Herring, *The Current Crisis in International Banking*, 8 BROOKINGS DISCUSSION PAPERS IN INTERNATIONAL ECONOMICS 30-31 (Dec. 1983).

90. Guttentag & Herring, *Current Crisis in International Banking*, *supra* note 89.

91. See *supra* note 19 and accompanying text.

92. See Wall St. J., Dec. 27, 1983, at 2, col. 3.

93. SEC, Staff Accounting Bulletin No. 56, Disclosure Concerning Mandated Reserves, 49 Fed. Reg. 4936 (1984) (to be codified at 17 C.F.R. § 211).

94. *Id.*

95. The new accounting requirements will not affect earnings over the long-term. For example,

suppose a bank extended \$1 billion in four-year loans every year, charging one percent in fees. The traditional method of including all fees as current income would allow the bank to declare \$10 million in underwriting earnings every year, beginning in the first year. Averaging would require the bank to report \$2.5 million, \$5 million, and \$7.5 million in . . . earnings in years one, two, and three, and \$10 million in every succeeding year. Thus the choice of method has a short-term effect on reported earnings but no long-term effect.

R. DALE & R. MATTIONE, *supra* note 13, at 39 n.69.

96. See Joint Memorandum, *supra* note 50, at 30.

C. NEW DISCLOSURE REQUIREMENTS

The Act's new disclosure provisions may prove to be the centerpiece of the reforms. The provisions make information on country exposure concentrations publicly available, thereby enabling market discipline to play a greater role in regulating bank exposures. The disclosure requirements parallel those the SEC recently adopted.⁹⁷ Consequently, the disclosures should not disrupt the market to any significant extent in the short term.

The question for the long term is whether markets will respond to routine disclosure so as to control overexposure *before* a crisis occurs. Some analysts doubt the ability of the market to respond soon enough or strongly enough to constrain lending.⁹⁸ In addition, governmental rescues of troubled banks further weaken the market's influence on lending practice.⁹⁹ On the other hand, some analysts argue that routine prior disclosure of lending data is less likely to be disruptive than sudden disclosure under crisis conditions and that subsequent disclosure is certain once a crisis develops.¹⁰⁰

As a complement to regulatory controls, market controls could reinforce regulators' efforts to contain country risk exposure. Regulatory controls alone have clearly proved ineffective. At the very least, more frequent reporting of lending data will make these controls more efficient. Nevertheless, the long-term effect of public disclosure on country lending concentrations remains unclear.

D. SHORT-TERM LENIENCY VERSUS LONG-TERM REFORM

The International Lending Supervision Act strikes a balance between long-term structural reform and short-term leniency to avoid disrupting private credit flows and exacerbating the current liquidity crisis. If anything, the reforms err on the side of leniency for the lending banks. As the pressure on the debtor nations grows, however, the wisdom of congressional leniency becomes increasingly suspect.¹⁰¹ So far, the rescheduling packages have provided little true debt relief. The losses from bad loans have been shifted to the debtor countries,

97. See *supra* note 69.

98. *To Increase the U.S. Quota*, *supra* note 20, at 208-09 (paper by Jack Guttentag & Richard Herring).

99. The highly-publicized rescue of the Continental Illinois Bank and Trust Company casts further doubt on the prospects for greater market controls on bank lending. See 42 WASH. FIN. REP. (BNA) No. 21, at 847 (May 21, 1984).

100. For a full analysis of disclosure policy, see Guttentag & Herring, *Disclosure Policy and International Banking*, *supra* note 84.

101. See Riding, *The New Crisis for Latin Debt*, N.Y. Times, Mar. 11, 1984, at 1F, 8F. See also Samuelson, *Do Banks Serve U.S. Interests?*, Wash. Post, Apr. 11, 1984, at F1, F8.

while banks have managed to protect their profits.¹⁰² Increasingly, U.S. commentators and representatives from the debtor countries question the wisdom and effectiveness of current lending policies. Without a restoration of economic growth, the debt-servicing capacity of Latin American and other developing countries cannot improve, and without a reduction in debt burdens, the prospects for economic recovery are bleak.¹⁰³ A reduction in interest charges and fees on current lending along with an extension of the maturity of outstanding loans will be necessary in order to end the cycle of economic stagnation in the debtor countries.¹⁰⁴

Over the long term, the ILSA is only an initial step toward controlling bank exposures to developing countries. On the positive side, the reforms recognize that basic structural problems exist and attempt to address them apart from the immediate liquidity crisis. The regulations encourage the reduction of country concentrations of bank loan exposures and provide some additional cushioning for the effect on bank balance sheets in the event the condition of the debtor countries does not improve. They also increase the availability of information regarding the financial condition of country borrowers. The impact of each of these changes, however, is yet to be felt. The legislation does not address a number of other significant issues which must play a role in any long-range solution to the debt problem. Among the most urgent are the need to reduce the debt burden of the debtor countries and to diminish the reliance on short-term commercial credit for current account financing.¹⁰⁵

102. See Samuelson, *supra* note 101. Each time loans are rolled-over, spreads and banks' profits are increased. Instead of adding to capital investment, current lending to Latin American countries is quickly recycled to cover interest payments on outstanding loans. Of the \$5.0 billion in new loans to Mexico in 1983, for example, \$3.5 billion went to cover the interest and fees on the new loan and the \$20 billion in rescheduled loans. The remaining \$1.5 billion went toward interest payments on rescheduled debt. *To Increase the U.S. Quota*, *supra* note 20, at 490 (statement of Karin Lissakers).

103. Ronald Leven and David Roberts note that high interest rates and low industrial country growth will prolong the recovery period. See *Latin America's Prospects for Recovery*, FED. RES. BANK N.Y.Q. REV., Autumn 1983, at 6. For a similar conclusion, see the analysis of prospects for Latin American recovery under alternative assumptions of interest rates and industrial country growth in T. ENDERS & R. MATTIONE, *LATIN AMERICA: THE CRISIS OF DEBT AND GROWTH* (1984).

104. See Samuelson, *supra* note 101; Silk, *Ending Latin Debt Crisis*, N.Y. Times, May 2, 1984, at D2, col. 1; T. ENDERS & R. MATTIONE, *supra* note 103.

105. Jack Guttentag and Richard Herring, in their study of international lending exposure, list these and other criteria for evaluating policy actions to deal with the debt crisis. See *To Increase the U.S. Quota*, *supra* note 20, at 195-96. Analysts have proposed a number of methods to stretch out the distressed countries' debt repayment schedules and to convert short-term credit to longer-term debt instruments. See generally, R. DALE & R. MATTIONE, *supra* note 13, for a discussion of several prominent proposals. See also Anthony M. Solomon, *Toward a More Resilient International Financial System*, FED. RES. BANK N.Y.Q. REV., Autumn 1983, at 1 (listing a number of nongovernmental initiatives for alleviating the debt crisis).

. An escalation of the liquidity and solvency problems of the debtor countries could increase significantly the impact of the new regulations on banks.¹⁰⁶ Growing resistance to the austerity programs and to high interest rates that were negotiated in the first round of restructuring threatens to erupt in a new crisis which may trigger a new series of adjustments within the financial system.¹⁰⁷

In the long run, tougher policies will undoubtedly be necessary to reduce bank exposure to developing countries. The degree to which these policies will require stronger regulatory measures will depend on the success of other efforts to address the problem. The extent of international cooperation achieved among banking supervisory systems will proportionately affect the success of U.S. controls.¹⁰⁸ Other proposals call for a greater role for the IMF in lending supervision¹⁰⁹ as well as for increased information sharing with banks¹¹⁰ and greater public disclosure.¹¹¹ Another factor that will determine the need for regulatory measures is the efficacy of market controls, which in part depends upon the amount of information available to investors and depositors. In addition, the success of independent prudential efforts adopted by banks themselves will determine the extent of needed regulatory controls.¹¹²

106. See *supra* notes 90-92 and accompanying text.

107. See Riding, *The New Crisis for Latin Debt*, N.Y. Times, Mar. 11, 1984, at 1F, col. 2, 8F, col. 1.

108. See Chan, *An International Code for Banking Supervision*, INT'L FIN. L. REV., July 1983, at 26-27 (on the report of the Cooke Committee to the Bank for International Settlements); Joint Memorandum, *supra* note 50, at 31.

109. See R. DALE & R. MATTIONE, *supra* note 13, at 33-34. These proposals call for continuous IMF involvement in monitoring developing-country borrowing strategies before problems emerge. Currently, the Fund intercedes only when the borrower experiences difficulties and applies for IMF assistance. Some proponents suggest that it would be possible to expand the Fund's surveillance responsibilities under the exchange-rate supervision authority granted in the IMF Articles of Agreement, given the impact of external debt on forming exchange-rate policies. *Id.* at 33 n.56.

110. *Id.* at 32-33. Some analysts express concern that greater information sharing might discourage disclosure by member countries to the IMF. *Id.*; M. MENDELSON, *supra* note 16, at 13.

111. The IMF is starting to disclose more complete data on international lending. In January 1984, the Fund added six new tables to its monthly publication, *International Financial Statistics*. The tables provide for the first time disaggregated data on international credit flows and deposits by country of borrower and lender. 42 WASH. FIN. REP. (BNA) No. 3, at 154 (Jan. 16, 1984). The IMF quota increase passed by Congress included a provision calling for more complete and timely exchange of financial data with members of the banking system as well as greater public information disclosure. Pub. L. No. 98-181, § 802 97 Stat. 1268 (to be codified at 22 U.S.C. § 286e-2).

112. In the second half of 1982, banks began increasing loan-loss reserves. *To Increase the U.S. Quota*, *supra* note 20, at 494 (statement of Karin Lissakers). The capital-to-loan ratios of the 17 largest banks rose from 4.39% at the end of 1980 to 5.02% at the end of 1982. *Id.* at 249 n.5 (statement of William R. Cline, Inst. for Int'l Economics).

As an alternative to greater governmental disclosure requirements, 36 banks from nine countries formed the Institute of International Finance (IIF) in early 1983. The institute intends to promote the exchange of economic and financial information between banks and

"[R]eplacing the banks as the principal vehicle for capital flows to developing countries will be the principal international financial challenge of the 1980's."¹¹³ The International Lending Supervision Act's contribution to reducing the overextension of U.S. banks will only be apparent several years hence. The Act takes an initial step toward controlling foreign lending in the longer term, while avoiding any measurable impact on current lending practice.

IV CONCLUSION

The global debt crisis that emerged in 1982-83 forced a legislative reappraisal of bank lending and banking regulation. Regulatory controls had proved inadequate to prevent the dangerous overexposure of U.S. banks to developing country borrowers. The International Lending Supervision Act imposes new controls on foreign lending designed to prevent a recurrence of the debt buildup. The existing large country debt concentrations, however, limited the available remedies. Legislators were forced to balance long-term structural reform with the need to preserve short-term commercial credit flows to distressed countries.

The International Lending Supervision Act takes an initial step toward controlling foreign lending exposure. While stronger measures undoubtedly will be necessary in the long run to effect a permanent resolution of the problem, the Act avoids the disruptive effect that more stringent controls might have had on the immediate payments crisis. At the same time, the reforms encourage the reduction of country concentrations of bank loan exposures and introduce greater market controls through more complete foreign lending disclosure. Comprehensive solutions to the global debt problem, however, will require more fundamental reforms.

Ellen W. Smith

borrowing countries. See *Global Economic Outlook: Hearings Before the Subcomm. on International Economic Policy of the Senate Comm. on Foreign Relations*, 98th Cong., 1st Sess. 76 (1983) (statement of William S. Ogden, interim chmn., IIF). Many bankers remain skeptical about the usefulness of the IIF. See M. MENDELSON, *supra* note 16, at 18, 34-36.

113. *To Increase the U.S. Quota*, *supra* note 20, at 252 (statement of William R. Cline).

